THIS OPINION IS NOT INTENDED FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

IN RE	)	CASE NO. 97-53509
	)	
DENNIS AND ALANA LEEK,	)	CHAPTER 7
	)	
	)	JUDGE MARILYN SHEA-STONUM
Debtors.	)	
	)	ORDER DENYING REQUEST TO
	)	SURCHARGE COLLATERAL
	)	PURSUANT TO 11 U.S.C. § 506(c)

This matter came before the Court on the First and Final Application of Attorney for Debtors/Debtors-In-Possession for Compensation and Reimbursement of Expenses/Motion for Payment Pursuant to 11 U.S.C. § 506(c) (the "Application"), filed by Roth, Blair, Roberts, Strasfeld & Lodge ("Applicant"), and the objection of the United States Trustee (the "UST") thereto. This matter is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A). This Court has jurisdiction over this matter pursuant to 28 U.S.C. § 157(a) and (b)(1) and by the Standing Order of Reference entered in this District on July 16, 1984.

I. FINDINGS OF FACT

A. The Filing and Conversion of the Debtors' Bankruptcy Case

On December 3, 1997, Dennis and Alana Leek (the "Debtors") filed a petition for relief under chapter 11 of the Bankruptcy Code. During the pendency of the chapter 11 proceeding, the Debtors allegedly established a "Post-Petition Chapter 11 Reorganization Account" (the "Account"). On November 12, 1998, the Debtors' case was converted to a chapter 7 proceeding.

B. The Employment of Applicant

On January 6, 1998, Applicant was employed as co-counsel for the Debtors. Applicant was not employed to act as lead bankruptcy counsel. Rather, the motion to employ Applicant stated that Applicant's employment was sought "to provide accounting services to the Debtors/Debtors-in-Possession during the pendency of this proceeding and so as to assist lead counsel in performing additional legal services as may be required but not duplicative."

C. The Relief Sought By Applicant

Pursuant to the Application, Applicant seeks compensation in the amount of $7,250.00 and expense reimbursement in the amount of $109.66 for the period of January 15, 1998 through October 29, 1998. To the extent that the funds in the Account constitute the collateral of Orix Credit Alliance, Inc. ("Orix") or the Internal Revenue Service (the "IRS"), pursuant to 11 U.S.C. § 506(c), Applicant seeks to be paid the lesser of Applicant's approved fees or 75% of the funds in the Account.[1] In support of obtaining payment from the funds in the Account, which may constitute the collateral of Orix and/or the IRS, Applicant contends that Orix and/or the IRS benefitted from Applicant's services because the Debtors' outstanding accounts receivable allegedly increased in the approximate amount of $12,000.00 during the pendency of the Debtors' chapter 11

---

[1] Although Applicant is seeking payment of its allowed fees and expenses from the alleged collateral of the IRS, Applicant did not serve the Application in the manner required for service upon the United States and its agencies under Fed. R. Bankr. P. 7004 and 9014. Consequently, even if Applicant had otherwise satisfied the standards for surcharge of a secured creditor's collateral pursuant to § 506(c), the Court would have to deny Applicant's request to surcharge any collateral of the IRS because of a deficiency in service.

[2] The Application states that the Debtors held $58,674.00 in outstanding accounts

proceeding.[2]

The UST objects to Applicant obtaining immediate payment from secured creditors' collateral pursuant to § 506(c). In addition, in a Motion of Orix Credit Alliance, Inc. for Accounting of Cash Collateral, Orix requested that an accounting of cash collateral be provided before the Court consider Applicant's request to surcharge collateral for payment of Applicant's allowed compensation. No other objections to the Application were filed.

The Court conducted two pre-hearing conferences on December 9, 1998 and January 20, 1999 regarding the appropriate time to schedule a hearing on the allowance of Applicant's fees and expenses and the objections regarding Applicant's request to surcharge. Notice of the two pre-hearing conferences was served on parties in interest and the UST. During the second of the two pre-hearing conferences, the Court advised the parties in interest who appeared at the conference that the Court would take the matter regarding Applicant's request to surcharge under advisement.

II CONCLUSIONS OF LAW

A. Award of Compensation and Reimbursement of Expenses

Pursuant to 11 U.S.C. § 330(a), after notice to parties in interest and the UST and a hearing, the Court may award Applicant reasonable compensation for actual, necessary services and reimbursement for actual, necessary expenses. In light of the Court's determination, as set forth below, that Applicant is not entitled to surcharge the funds in the Account, and the conversion of the Debtors' case to a proceeding under chapter 7, the Court will rule on the allowance of Applicant's fees and expenses, to the extent necessary, at the final meeting for the Debtors' chapter 7 proceeding.

---

receivable at the time of their bankruptcy filing and held accounts receivable in the amount of $70,601.93 as of August 1998.

B. Entitlement of Applicant to Surcharge Collateral

Section 506(c) provides that "the trustee may recover from property securing an allowed secured claim the reasonable, necessary costs and expenses of preserving, or disposing of, such property to the extent of any benefit to the holder of such claim."[3] 11 U.S.C. § 506(c). Three elements must be present in order to surcharge a secured creditor with administrative expenses pursuant to § 506(c): (1) the expense must be necessary for the preservation or the disposal of the collateral, (2) the amount of the expense must be reasonable, and (3) the secured creditor must benefit from the expense. In re Great Northern Forest Products, 135 B.R. at 70. The party seeking recovery bears the burden of proving that § 506(c) is applicable. In re Ferncrest Court Partners, Ltd., 66 F.3d 778, 782 (6th Cir. 1995); In re Williamson, 94 B.R. 958, 962 (Bankr. S.D. Ohio 1988). Thus, the party seeking to surcharge must prove, by a preponderance of the evidence, "a direct quantifiable benefit to the secured creditor which enabled the secured creditor to realize as much or more than it would have had it enforced its security interest outside of bankruptcy . . . ." In re Glen Eden Hosp., Inc., 202 B.R. 589, 590 (Bankr. E.D. Mich.

---

[3] In its objection, the UST contends that Applicant does not have standing to seek surcharge pursuant to § 506(c). See, e.g., In re Dyac Corp., 164 B.R. 574, 581 (N.D. Ohio 1994)(holding that debtor's accountant did not have standing to surcharge a secured creditor's collateral pursuant to § 506(c)); In re Kessler, Inc., 142 B.R. 796, 800 (W.D. Mich. 1992)(holding that debtor's counsel did not have standing to bring a claim under § 506(c)); In re Great Northern Forest Products, 135 B.R. 46, 70 (Bankr. W.D. Mich. 1991)(holding that debtor's landlord did not have standing to surcharge a secured creditor's collateral pursuant to § 506(c)). Contra Equitable Gas Co. v. Equibank (In re McKeesport Steel Castings Co.), 799 F.2d 91, 94 (3d Cir. 1986); In re Staunton Indus., 74 B.R. 501, 506 (Bankr. E.D. Mich. 1987)(holding that landlords had standing to surcharge); In re Wyckoff, 52 B.R. 164, 167 (Bankr. W.D. Mich. 1985)(same). Given that the Court finds that Applicant has not satisfied the requirements pursuant to § 506(c) for surcharging what may be the collateral of Orix and/or the IRS, the Court makes no determination as to whether or not Applicant has standing to do so.

1995)(denying administrative claimants' request to surcharge accounts receivable in which Internal Revenue Service held a security interest because claimants "failed to establish that their services provided a direct benefit to the IRS"). See also In re Staunton Indus., 75 B.R. 699, 702 (Bankr. E.D. Mich. 1987)(denying landlords' request to surcharge collateral for payment of post-petition rents owed because landlords failed to prove that secured creditor received a direct quantifiable benefit from debtor's use of landlords' property).

When a court has determined that counsel to a debtor in possession was entitled to surcharge a secured creditor's collateral pursuant to § 506(c), the court has noted that the efforts of the debtor's counsel specifically related to the collateral to be surcharged and directly benefitted the secured creditor. For example, in In re Croton River Club, 162 B.R. 656 (Bankr. S.D.N.Y. 1993), which Applicant cites in support of its request to surcharge, the debtor's counsel represented the debtor in trial and appellate litigation which resulted in a permanent and substantial reduction in the related collateral's operating expenses. The collateral sold at auction for $715,000. The court determined that, but for the successful litigation efforts of the debtor's counsel, the secured creditor's collateral could not have been sold and thus found that, because of the efforts of the debtor's counsel, the secured creditor had received a benefit in the amount of $715,000 (the collateral's sale price).

With respect to the case at hand, Applicant has failed to establish its satisfaction of each of the elements of § 506(c). Notably, Applicant has not established that any funds in the Account actually constitute the collateral of Orix and/or the IRS. Second, even if those funds do constitute the collateral of Orix and/or the IRS, Applicant has not established that Applicant's efforts were necessary to preserve the funds, i.e., that the tasks for which Applicant seeks to be compensated were responsible for the generation of the funds. For example, if the funds constitute the proceeds of the Debtors' accounts

receivable (which were generated after Applicant was employed), the Debtors, not Applicant, are likely responsible for the creation and collection of those accounts receivable. Third, Applicant has not shown that Orix and/or the IRS benefitted from the tasks for which Applicant seeks to be compensated. Even if the Debtors' accounts receivable did increase during the pendency of their chapter 11 proceeding, and Applicant's efforts are directly responsible for that increase, the latter assumption being unsupported by any record evidence, Orix and/or the IRS did not necessarily benefit from an increase in the face amount of the Debtor's post-petition accounts receivable. The Debtors' post-petition accounts receivable may not be fully (if at all) collectible and thus may have a realizable value which is far less than their face amount.

Given that Applicant has failed to meet its burden of proving that each of the elements of § 506(c) is satisfied, the Court holds that, absent further Order from the Court, Applicant may not be paid its allowed fees and expenses from any funds in the Account. Such relief might be granted if Applicant were to establish that: (1) the funds to be used in the Account constitute the collateral of a creditor which has an allowed secured claim and which has consented to Applicant being paid from those funds or (2), if the funds do not constitute the collateral of a creditor which has an allowed secured claim, sufficient funds exist to pay allowed chapter 7 administrative claims in full prior to Applicant being paid from any funds in the Account.

IT IS SO ORDERED.

_____
MARILYN SHEA-STONUM
Bankruptcy Judge

DATED: 3/1/99